

EQUITY

Global Equities

Alongside signs that higher prices could become entrenched in consumers' expectations, the US Federal Reserve (Fed) hiked interest rates by 75 basis points (bps) during its June 2022 policy meeting, the first move of such magnitude since 1994. Other central banks also surprised the market with more hawkish actions. Market movements: US (-6.7%), Hong Kong (+2.1%), Shanghai (+6.7%), Japan (-3.3%), Korea (-13.2%), Taiwan (-11.8%), Eurozone (-8.8%), Singapore (-4.0%), Thailand (-5.7%), Indonesia (-3.3%), and Malaysia (-8.0%).

US

In the US, the 'peak inflation' narrative for the US was swept aside by the release of the May 2022 CPI print last month. The Fed raised its Fed funds interest rate by 75bps to 1.50-1.75% to curb US inflation running at four-decade highs of 8.6%. This was the Fed's first 75bps rate increase since 1994. Markets are now increasingly weighing the possibility of a recession given higher interest rates and tighter financial conditions. The potential impact on consumer spending from any reversal in the low US unemployment levels that is seen today needs to be monitored.

Europe

Europe is still being impacted by shocks. The war in Ukraine has amplified an inflation shock that was already larger than anticipated, and the sharp fall in consumer confidence is concerning. There is a risk that the surge in inflation leads to second-round effects via wages and inflation expectations, which would call for a more aggressive European Central Bank response. Supply bottlenecks have proved longer-lasting, leading to a slower recovery in manufacturing, with China's zero-Covid policy being another risk. The threat of a disruption in gas supplies also remains significant.

China

Although there are concerns about China's slowing growth given little clarity on when and how quickly its strict zero-Covid policy might be relaxed, supportive policy momentum has gathered pace. After launching the passenger vehicles purchase tax cut, President Xi mentioned of support to internet and platform companies and reiterate the commitment to economic targets. At the industry level, the Ministry of Finance announced subsidies to local provinces developing solar and wind power infrastructure as part of the effort to support renewables development. The latest economic data highlighted modest recovery in activities and retail sales though overall consumption sentiment would still be cautious.

Asia

Malaysia performed worse than many regional peers, with the FBMKLCI declining by 8%, driven by global slowdown concerns and tighter monetary policies. Rising inflationary pressures came to the fore with the May CPI print recording a year-on-year increase of 2.8%, while CPO price experienced a sharp fall, hurting the plantation players. No sector recorded a gain during the month. A key event to watch in July will be the Bank Negara Malaysia's MPC meeting. Economic growth is expected to maintain its course on the back of robust private consumption following the economy reopening and labour market improvement, although rising inflationary pressures coupled with a higher interest rate environment could slow the pace.

General View

As we head into the second half of 2022, fears that the global economy could slip into recession continue to dominate headlines. The path of inflation remains a key source of uncertainty for markets for which global central banks are expected to maintain their aggressive rate hike trajectories in the months ahead. Heightened risks of recession would consequently lead to corporate earnings declines, which would further weigh on risk asset prices. The uncertainty calls for a much more selective investment approach focusing on quality, resilience and diversification. We maintain our Neutral stance on local equities, as positive economic recovery for the year is being challenged by headwinds in the form of rising global inflationary risks, weaker Ringgit and dampening business and consumer sentiment which would affect next year's earnings prospects.

FIXED INCOME

US Treasuries

Financial markets are experiencing heightened volatility and tighter financial conditions as central banks employ more restrictive monetary policies due to persistent inflation. The 2-year/10-year Treasury bond yield curve briefly inverted in mid-June as the 2-year rates surged to a 15-year high while the 10-year Treasury yield rose to an 11-year high of almost 3.50% before declining to the 3% level. The Federal Reserve (Fed) raised rates by 0.75%, its largest increase in 28 years as deteriorating inflation outlook forced the US central bank to increase rates more rapidly to combat inflation that is running at a 40-year high. In his statement regarding Fed policy, chairman Jerome Powell was keen to point out that while a further 75 basis points (bps) hike next month was possible, hikes of this magnitude would not become "common"; nevertheless, the central bank would have to "act with flexibility". Concurrently, economic growth was revised lower for this year and for 2023 and 2024. Towards month-end, yield movements continue to signal stalling growth momentum retreating from multi-year highs, sparking markets to reduce expectations for Fed rate hikes. The 2-year yield rose by 31bps to 2.95% while the 10-year yield rose 10bps to 3.01%.

Malaysian Bond Market

Back home, local government bonds saw better buying support during the month as the late month rally seen in US Treasuries alongside global rates spurred buying activities. Bond sentiment remains dominated by global inflation and rate drivers which added to further volatility throughout the month. Despite starting the month on a weaker footing, yields retreated from the peak in mid-June to close the month moderately higher by 2-20bps with the bulk of the weakness concentrated on papers of medium tenure. Demand for duration improved with government auctions drawing strong BTC of 2.21x and 2.45x for the 15-year and 30-year MGS auctions respectively. The 5-year GII reopening auction received an overwhelming demand of 3.13x given the slightly smaller than anticipated issue size. Elsewhere, Malaysia's Consumer Price Index rose 2.8% year-on-year for the month of May, surpassing initial estimates of 2.6% as well as April's reading of 2.3% owing to higher food and transportation prices. In view of the larger quantum of Fed rate hikes and the looming inflationary pressures, we expect Bank Negara Malaysia (BNM) to step up its policy normalization measures where markets are currently expecting a cumulative increase of 50bps in 2H2022. Over the month, the MGS curve saw a bear flattening move with the 3-year adjusting 5bps higher to 3.52% while the 10-year was marginally higher by 2bps to 4.26%.

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